

Mahanagar Gas Ltd



RESULT UPDATE

13th May, 2019

Mahanagar Gas Ltd

Higher opex hit margins

CMP INR 854	Target INR 1,036	Potential Upside 21.3%	Market Cap (INR Mn) 84,341	Recommendation BUY	Sector Oil & Gas
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Result highlights

Net sales came at INR 7.2 bn, (+23.1% YoY and -4.0% QoQ) driven by higher realizations but lower CNG and domestic PNG volumes on a YoY basis. Total sales volume for Q4 registered a growth of 7.4% YoY while declining by 0.74% QoQ primarily due to lost CNG volumes (-1.1% QoQ). Gross margins declined to 49.3% on a YoY basis (-109 bps) due to higher gas costs (+25.8% YoY) and a higher excise duty out-go (+24.5% YoY). OPM was further negatively impacted (-40 bps YoY, -216 bps QoQ) to 29.6% owing to higher employee costs (+15.0% YoY, +6.2% QoQ) and other expenses (+19.6% YoY, +9.7% QoQ). EBITDA stood at INR 2.1 bn. (+21.5% YoY, -10.5% QoQ). Lower finance cost (-44.4% YoY, -16.7%) and higher other income (+37.3% YoY, +16.9% QoQ) aided PAT at INR 1.3 bn (+27.4% YoY, -10.0% QoQ). The tax rate remained nearly unchanged at 34.9%. NPM declined by 123 bps QoQ while increasing by 62 bps YoY to 18.5%. The board has recommended a dividend of INR 10.5 per share on a FV of INR 10.

MARKET DATA

Shares outs (Mn)	98
Equity Cap (INR Mn)	988
Mkt Cap (INR Mn)	87808
52 Wk H/L (INR)	1057/757
Volume Avg (3m K)	433
Face Value (INR)	10
Bloomberg Code	MAHGL IN

KEY FINANCIALS

Particulars (INR Mn)	FY17	FY18	FY19	FY20E	FY21E
Revenue from Operations	20,340	22,330	27,911	30,142	34,212
EBITDA	6,442	7,801	8,855	9,474	10,754
PAT	3,934	4,779	5,464	5,687	6,397
EPS Diluted (Rs.)	39.83	48.38	55.32	57.57	64.76
OPM	31.7%	34.9%	31.7%	31.4%	31.4%
NPM	19.3%	21.4%	19.6%	18.9%	18.7%
P/E (x)	21.4	17.7	15.4	14.8	13.2

Source: Company, KRChoksey Research

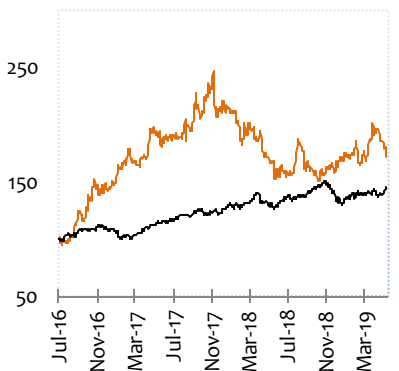
Volume growth remains subdued; Realizations may remain constrained

Total Q4FY19 sales volumes grew 7.4% YoY while remained flat (-0.74%) on a QoQ basis, with growth of 6.9%/9.0% YoY for CNG/PNG, respectively with volumes at 3.01 mmscmd – 2.20/0.81 for CNG/PNG. However, CNG volumes de-grew on a QoQ basis (-1.13%) attributed to lower number of days in the quarter and strike by BEST services which impacted CNG offtake. For PNG segment, industrial & commercial (I&C) sales grew 8.6% YoY (+1.5% QoQ) while domestic segment grew 9.6% YoY but declined 0.91% QoQ likely due to rise in APM prices leading to higher PNG realizations thereby making it less competitive vis-à-vis LPG cylinders for households. Despite lower spot gas prices, I&C realizations came lower with management attributing it to indexing realizations with a lag thereby impacting gross margin (-109 bps YoY). Full year volume growth remained robust at 9.2%, in-line with management's growth guidance. We believe, even if the volume growth momentum continues, the recent hike in APM gas prices (+9.8%) may call for higher realizations making domestic gas consumption less attractive hence keeping margins under pressure. However, decline in spot prices may help improve boost revenues from I&C segment. We remain in-synch in management's volume guidance of 6-7%. We estimate total volumes at 3.2 and 3.5 mmscmd for FY20/21E respectively.

Higher opex hits operating margins

Even with lower spot prices and a stronger rupee, EBITDA/scm came lower at INR 7.91/scm, down 9.9% QoQ on account of higher opex including provisions (inventory-related, pipeline-related) and lower realizations in industrial segment. Other expenses came in higher, up 19.6% YoY and 9.7% QoQ attributed to increasing variable expenses (power & fuel, CNG dispensing charges) with rising volumes in GA3 (Raigad). Q4 expenses also included provisions of ~INR 6 crore related to inventory and pipeline. For FY19, EBITDA/scm reported strong at INR 8.22/scm (INR 7.91 in FY18). Management has stated that the opex

SHARE PRICE PERFORMANCE



— Mahanagar Gas Ltd — Sensex

MARKET INFO

SENSEX	37,091
NIFTY	11,148

SHARE HOLDING PATTERN (%)

Particulars	Mar 19	Dec 18	Sep 18
Promoters	42.5	42.5	42.5
FIIIs	24.36	21.61	19.03
DIIIs	12.86	13.4	14.25
Others	20.28	22.5	24.23
Total	100	100	100

10.8%

Revenues CAGR between FY 19 and FY 21E

10.2%

EBITDA between FY 19 and FY 21E

ANALYST

Neha Raichura, neha.raichura@krchoksey.com, +91-22-6696 5590

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Thomson Reuters, Factset and Capital IQ

Phone: +91-22-6696 5555 / Fax: +91-22-6691 9576
www.krchoksey.com

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run-rate will likely continue with increasing operations and with on-going infrastructure expansion in GA3. We expect EBITDA margins to bounce back, although not at very high levels, from lower spot gas prices and lesser or no provisions as was in Q4. We estimate EBITDA levels between INR 8-8.5/scm for FY20/21E.

Operations expand in Raigad; Future opportunities remain to be seen

With increasing urbanization and rising penetration, we can expect an uptick in volumes from Raigad. As of Q4, 10 CNG stations were operational in the region and MGL plans to target another 10 in FY20. For the initial period, gas would be supplied through cascades in accord with MGL's low-investment high-yield strategy for Raigad, post which MGL plans to set up steel pipeline infrastructure. As for MGL's future growth prospects, it had applied for 2 GAs in the 10th PNGRB round launched in Nov'18 covering 50 GAs. However, it remained unsuccessful in obtaining any licenses due to more aggressive bids by other players, as cited by the management. However, management mentioned that it is open to both organic and inorganic opportunities in the future. We remain watchful of the kind of projects MGL takes up and how it unfolds, going forward, given that it's sizeable cash/bank balance at INR 2.98 bn (0.9 bn in FY18). Capex guidance for FY20 stood at INR 4.5 bn (INR 3.6 bn in FY19).

Valuation & Outlook:

Although we have a positive outlook on the sector with respect to the demand for NG, rising APM gas price coupled with a possibility of declined allocation of APM gas may affect operational performance keeping operating margins under pressure. Moreover, it may not always be a smooth move to pass on rise in gas costs to end consumers rendering CNG/PNG usage uncompetitive. The strong volume growth momentum, especially in CNG can provide some thrust. Few auto companies have recently announced phasing out of diesel vehicles on account of economic feasibility post BS-VI norms, which could trigger a demand for CNG vehicles leading to uptick in volumes. As for MGL's existing operations, the infrastructure exclusivity for Mumbai ends in May'20 and thus the nature of progress of operations (if MGL is declared a common carrier) remains to be seen. While the management has stated that it is open to both organic and inorganic opportunities, we await a further clarity on the MGL's future projects. We have revised our estimates to factor in the changes in gas prices and business development in the near future. We expect the revenues to grow at a CAGR of 10.8% over FY19-21E and EBITDA to grow at a CAGR of 10.2% over FY19-21E. At a CMP of INR 854, the stock is trading at 14.8x of its FY20E earnings and at 13.2x of its FY21E earnings. **We valued the company by assigning a multiple of 18x on the FY20E EPs of INR 57.6 and arrived at target price of INR 1,036 (from INR 1,146 earlier) with a potential upside of 21.3%. We maintain BUY rating on the stock.**

FINANCIALS PERSCM

	Q4FY18	Q3FY19	Q4FY19	Y-o-Y (%)	Q-o-Q (%)
Sales (INR/scm)	23.1	27.6	26.7	15.6%	-3.3%
Cost of gas (INR/scm)	11.6	14.1	13.5	17.1%	-3.7%
EBITDA (INR/scm)	7.0	8.8	7.9	13.0%	-9.9%

Source: Company, KRChoksey Research

SALES VOLUME PERFORMANCE

	Q4FY18	Q3FY19	Q4FY19	Y-o-Y (%)	Q-o-Q (%)
CNG (mmscm)	184.9	199.8	197.6	6.9%	-1.1%
PNG (mmscm)	66.9	72.7	72.9	9.0%	0.3%

Source: Company, KRChoksey Research

GAS SALES REALIZATION

	FY16	FY17	FY18	FY19	FY20E	FY21E
CNG realization (INR/scm)	22.2	20.7	21.2	23.8	26.7	28.5
PNG realization (INR/scm)	26.0	23.9	26.6	30.9	31.8	32.4

Source: Company, KRChoksey Research

GAS SALES VOLUMES

	FY16	FY17	FY18	FY19E	FY20E	FY21E
CNG (mmscm)	660	693	724	791	865	929
PNG (mmscm)	230	244	262	286	315	342

Source: Company, KRChoksey Research

ANALYST

Neha Raichura, neha.raichura@krchoksey.com, +91-22-6696 5590

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Q4FY19 Concall Highlights:

- MGL had applied for 2 Gas namely Mysuru, Mandya districts and Alapuzha, Kullam and Trivandrum districts under the 10th CGD bidding round. It did not succeed in winning any of these Gas
- Raigad GA - it has 8,900 domestic connections in Uran and adjoining areas. Gas supplied to major towns like Uran, Pen and Karjat is being planned through the virtual pipeline network to begin with. 3 CNG stations were added during the quarter and with this, 10 CNG stations are currently operational in Raigad.
- EBITDA declined to INR 7.91/scm v/s INR 8.77/scm in Q3FY19 due to lower I&C sales realizations, higher optics for CSR and repairs & provisions.
- Other expenses increased QoQ due to INR 6 cr of provisions (inventory-related, pipeline related which may not be monetized immediately) and provisions due to new AS. Other reasons are increase in O&M activities. Opex in Q3/Q4 is generally higher than in Q1/Q2.
- Substantial amount of opex is variable such as power & fuel, dispensing charges, consumption of stores & spares which rise with volumes. Also, LCV transportation charges on which cascades carrying CNG are mounted are used where online CNG stations are not available have increased in Q4 for Raigad. As a thumb rule, on an average, opex can be expected to rise by 12-13% with rise in volumes, although trend may differ.
- Guidance on overall volumes are maintained at 6-7% growth – CNG 6-7%, Domestic & Commercial – 7-8%, Industrial - 5-6%.
- CNG stations targeted for FY20 are 25 (including Raigad 5-10). Guidance on household connection to be added can be 1.1-1.2 lakh.
- BEST buses consumption – total CNG 1,800 buses which consume ~55 kgs/day/bus, which comes to 1 lakh kgs per day.
- Despite oil price levels being down in Q4 v/s Q3 and prices in I&C segment prices are indexed with a lag (about 1 month), gross margins got impacted. Now with lower spot gas prices, it can be expected to improve in next quarters, barring fluctuations in forex.
- Average spot gas prices in Q4: \$<9/mmbtu v/s Q3: \$10/mmbtu
- Capex for FY19: INR 360 crores FY20: INR 450 crores
- In short-term, it does not see too much of risk of EVs. There could be some penetration in near-term, however it could be more at expense of diesel and not CNG. On a pilot basis, MMRDA and BEST ran a trial for ~20 buses in Mumbai which was a commercial failure due to lack of ticketing revenue and adequate charging infrastructure.
- In case new entrant enters GA1 and uses MGL infrastructure - tariff regulations will be determined by PNGRB to be paid from new entrant to MGL. Previous regulations offered a 14% post-tax return on the regulated assets – thus tariffs may be set at that level.
- Regulations require entities to maintain 25% extra capacity to accommodate 3rd party commodity sellers. Many CGDs have completed their marketing exclusivity, but there have not been cases of 3rd entity entering for CGD. As of now, PNGRB has not declared MGL as a common carrier hence infrastructure cannot be used by 3rd party. There is also a provision for rollover of the exclusivity in blocks of 10 years which it expects to get for GA1.
- CNG conversions have been steady at 6-7k/month – 4-5k of it comes from autos while rest comes from private vehicles and aggregators. Numbers from trucks and CVs are very low.
- For Raigad district, CNG supply will initially be through cascades. After 1-2 years, steel pipelines and CG stations will be operational. Potential in Raigad – 0.6-0.7 mmscmd.

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QUARTERLY PERFORMANCE

Particulars (INR mn)	Q4FY19	Q3FY19	Q4FY18	QoQ (%)	YoY (%)
Revenue from operations	7,225	7,527	5,870	-4.0%	23.1%
Cost of natural gas & traded items	3,665	3,836	2,914	-4.5%	25.8%
Change in inventories	1	-1	-0	-162.5%	-600.0%
Cost of goods sold	3,665	3,835	2,914	-4.4%	25.8%
Gross Profit	3,560	3,692	2,956	-3.6%	20.4%
Gross Margin (%)	49.3%	49.1%	50.4%	22 bps	-109 bps
Employee benefit expenses	185	175	161	6.2%	15.0%
Other expenses	1,235	1,127	1,033	9.7%	19.6%
Total Operating Expenses	1,421	1,301	1,194	9.2%	18.9%
EBITDA	2,140	2,391	1,762	-10.5%	21.5%
EBITDA Margin (%)	29.6%	31.8%	30.0%	-216 bps	-40 bps
Depreciation	329	328	339	0.3%	-3.2%
EBIT	1,811	2,063	1,422	-12.2%	27.3%
Finance Cost	1	1	1	-44.4%	-16.7%
Other Income	238	204	174	16.9%	37.3%
Profit before tax	2,049	2,266	1,595	-9.6%	28.4%
Tax Expenses	714	783	548	-8.8%	30.4%
Adjusted Profit after Tax (PAT)	1,335	1,483	1,048	-10.0%	27.4%
PAT Margin (%)	18.5%	19.7%	17.8%	-123 bps	62 bps
Adj. EPS (INR)	13.51	15.02	10.61		

Source: Company, KRChoksey Research

INCOME STATEMENT

Particulars (INR mn)	FY17	FY18	FY19	FY20E	FY21E
Revenue from Operations	20,340	22,330	27,911	30,142	34,212
Cost of good sold	10,184	10,291	13,991	15,372	17,448
Gross Profit	10,156	12,039	13,920	14,770	16,764
Gross Margin (%)	49.9%	53.9%	49.9%	49.0%	49.0%
Employee benefit expenses	600	670	709	773	877
Other expenses	3,114	3,568	4,356	4,522	5,133
Total Operating Expense	3,714	4,238	5,065	5,295	6,010
EBITDA	6,442	7,801	8,855	9,474	10,754
EBITDA Margin (%)	31.7%	34.9%	31.7%	31.4%	31.4%
Depreciation	951	1,112	1,259	1,638	1,965
EBIT	5,490	6,689	7,596	7,837	8,788
Finance Cost	10	1	3	0	0
Other Income	527	577	777	892	1,031
Profit before Tax (PBT)	6,007	7,265	8,370	8,729	9,820
Total Tax expense	2,072	2,487	2,905	3,042	3,422
Profit after Tax (PAT)	3,934	4,779	5,464	5,687	6,397
PAT Margin (%)	19.3%	21.4%	19.6%	18.9%	18.7%
EPS Basic (INR)	39.83	48.38	55.32	57.57	64.76

Source: Company, KRChoksey Research

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Neha Raichura, neha.raichura@krchoksey.com, +91-22-6696 5590

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BALANCE SHEET

Particulars (INR mn)	FY17	FY18	FY19	FY20E	FY21E
EQUITY AND LIABILITIES					
Share capital	988	988	988	988	988
Reserves and surplus	17,413	19,966	23,001	27,403	32,354
Total Equity	18,400	20,953	23,989	28,390	33,342
Non-current liabilities					
Long term borrowings	27	12	0	0	0
Long term provisions	140	148	143	155	176
Other non-current liabilities	1,378	1,757	2,067	2,067	2,067
Total non-current liabilities	1,545	1,916	2,210	2,221	2,242
Current liabilities					
Trade Payables	1,201	1,100	1,524	1,646	1,869
Other Financial Liabilities	4,629	5,688	6,174	6,683	7,586
Short term provisions	67	51	69	74	85
Other Current liabilities	401	393	445	481	545
Total current liabilities	6,297	7,233	8,212	8,885	10,084
SOURCES OF FUNDS	26,243	30,102	34,410	39,497	45,668
ASSETS					
Non-current assets					
Net Block	17,163	18,886	21,331	25,323	29,425
Financial Assets	225	431	196	212	241
Other non-current assets	895	1,031	1,124	1,189	1,304
Total non-current assets	18,283	20,347	22,651	26,724	30,971
Current Assets					
Inventories	238	240	191	207	235
Other Financial Assets	6,021	8,425	8,396	9,087	10,314
Cash and bank balances	1,481	919	2,988	3,281	3,924
Other current assets	220	172	183	198	224
Total current assets	7,959	9,755	11,759	12,773	14,697
APPLICATION OF FUNDS	26,243	30,102	34,410	39,497	45,668

Source: Company, KRChoksey Research

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CASH FLOW STATEMENT

Particulars (INR mn)	FY17	FY18	FY19	FY20E	FY21E
Profit before Tax (PBT)	6,007	7,265	8,370	8,729	9,820
Operating profit before working capital changes	6,604	7,983	8,438	10,366	11,785
Cash Generated from/(used in) operations	7,329	8,805	7,638	10,789	12,535
Less: Income Tax Paid (net of refunds)	-1,862	-2,284	-2,905	-3,042	-3,422
Net Cash generated from/(used in) operating activities	5,467	6,521	4,733	7,746	9,113
Net Cash Used In Investing Activities	-2,777	-4,187	-3,368	-6,169	-7,024
Net Cash Used in Financing Activities	-2,838	-2,258	-1,250	-1,285	-1,446
Net Increase/(Decrease) in Cash and Cash Equivalents	-148	76	115	292	643
Cash and Cash Equivalents at the beginning of the year	222	74	150	265	558
Cash and Cash Equivalents at the end of the year	74	150	265	558	1,201
Add: Bank Balance	1,407	769	2,723	2,723	2,723
Cash & Bank balance	1,481	919	2,988	3,281	3,924

Source: Company, KRChoksey Research

RATIOS

Particulars	FY17	FY18	FY19	FY20E	FY21E
<u>Profitability</u>					
Return on Assets (%)	15.0%	15.9%	15.9%	14.4%	14.0%
Return on Capital (%)	29.8%	31.9%	31.7%	27.6%	26.4%
Return on Equity (%)	21.4%	22.8%	22.8%	20.0%	19.2%
<u>Margin Trend</u>					
Gross Margin (%)	49.9%	53.9%	49.9%	49.0%	0.0%
EBITDA Margin (%)	31.7%	34.9%	31.7%	31.4%	31.4%
Net Margin (%)	19.3%	21.4%	19.6%	18.9%	18.7%
<u>Liquidity</u>					
Current Ratio	1.3	1.3	1.4	1.4	1.5
Quick Ratio	0.4	0.3	0.5	0.5	0.5
Debtor Days	17	15	13	13	13
Inventory Days	4	4	3	3	3
Creditor Days	22	18	20	20	20
Working Capital Days	0	1	-4	-4	-4
<u>Solvency</u>					
Total Debt / Equity	0.0	0.0	0.0	0.0	0.0
Interest Coverage	538	7432	2374	NM	NM
<u>Valuation Ratios</u>					
EV/EBITDA	12.87	10.70	9.19	8.56	7.48
P/E	21.4	17.7	15.4	14.8	13.2
P/B	4.6	4.0	3.5	3.0	2.5

Source: Company, KRChoksey Research

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Mahanagar Gas Ltd				Rating Legend	
Date	CMP (INR)	TP (INR)	Recommendation	Our Rating	Upside
13-May-19	854	1,036	BUY	Buy	More than 15%
1-Feb-19	921	1,146	BUY	Accumulate	5% – 15%
8-Aug-18	961	1,182	BUY	Hold	0 – 5%
28-May-18	833	940	BUY	Reduce	-5% – 0
14-Feb-18	1,046	1,280	BUY	Sell	Less than – 5%
10-Nov-17	1,159	1,400	BUY		

ANALYST CERTIFICATION:

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Kisan Ratilal Choksey Shares and Securities Pvt. Ltd

Registered Office:

1102, Stock Exchange Tower, Dalal Street, Fort, Mumbai – 400 001.
Phone: +91-22-6633 5000; Fax: +91-22-6633 8060.

Corporate Office:

ABHISHEK, 5th Floor, Link Road, Andheri (W), Mumbai – 400 053.
Phone: +91-22-6696 5555; Fax: +91-22-6691 9576.

ANALYST

Neha Raichura, neha.raichura@krchoksey.com, +91-22-6696 5590

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Phone: +91-22-6696 5555 / Fax: +91-22-6691 9576
www.krchoksey.com